

BILL # HB 2585

TITLE: military sales tax exemption

SPONSOR: Weiers, JP

STATUS: As Introduced

REQUESTED BY: House

PREPARED BY: Eric Jorgensen

FISCAL ANALYSIS

Description

HB 2585 would exempt all retail sales to Regular, Reserve or National Guard components of the United States military from the Transaction Privilege Tax (TPT) and Use Tax requirements.

Estimated Impact

The JLBC Staff estimates that the bill would have a direct General Fund revenue loss of between \$7 million and \$30 million. The broad range is due to the lack of definitive information on military TPT purchases. The Arizona Department of Revenue did not provide a fiscal impact.

The bill could have some offsetting revenue impact if it aids the state's efforts in retaining its current military bases.

Analysis

Due to federal law, sales taxes cannot be levied against the federal governments or other sovereign nations. However, since Arizona has a Transaction Privilege Tax instead of a sales tax, federal government purchases are not exempt from taxation. The TPT allows the state to collect taxes on sales to the federal government by shifting the responsibility for the payment of the tax from the buyer to the seller. This bill exempts all retail sales made to the US military from taxation under the TPT and the Use taxes. Currently, only sales by a manufacturer, modifier, assembler or repairer are completely exempt from the TPT. All other sales to federal government entities are taxed at 50% of the TPT.

The exact amount of TPT collected from the military establishment, or from any individual or business is unknown. Nevertheless, some estimates can be made based on public information and assumptions about current military spending patterns.

In FY 2003, the most recent year available, the Department of Defense and its components (Army, Air Force, etc.) spent \$7.6 billion on procurement contracts in the state of Arizona. Because this bill would only exempt retail sales not already exempt from the TPT, the entire amount is not considered in the estimate. Rather, based on an educated guess about purchasing trends, JLBC Staff estimates that as much as 20% of the procurement budget may be spent on currently taxed retail items. This provides a tax base as high as \$1.6 billion.

The Department of Emergency and Military Affairs (DEMA), which administers the National Guard in Arizona, estimates the retail portion of their procurement budget at about \$1 million, or 33% of their non-salary budget. It is expected that retail would be a somewhat higher percentage of total procurement for the National Guard than for regular components because of the lack of defense contracts.

Officials at Luke Air Force Base estimate that up to 35% of procurement at the five military bases are currently taxed under the TPT. However, this figure would include more than just retail purchases. Using data from the government purchase card system, they found that on the \$1 million spent by Luke using these cards, about 5% was taxed under the TPT as retail. Applying this 5% factor to the statewide military procurement base of \$7.6 billion would result in a tax base of \$400 million.

Calculated on the upper limit tax base of \$1.6 billion, the lost revenues are approximately \$40 million. This is calculated by applying a tax rate of 2.5% to the base. The total TPT rate is 5.0% (excluding the 0.6% enacted by Proposition 301 – Education 2000); however, federal retail purchase are already discounted 50%. Exempting military retail purchases from the

remaining 50% will result in a state revenue loss of \$30 million to the General Fund with the remaining loss distributed to local governments.

Using a lower limit tax base of \$400 million, lost revenues are approximately \$10 million, with a state General Fund loss of \$7 million.

By reducing the federal government's operational cost, the bill may aid efforts to retain the state's military bases. In other states with a traditional sales tax, the military is exempt from taxation due to federal law.

Local Government Impact

TPT revenues are shared with local governments and any reduction in these collections would result in decreased funding for local governments. The estimated impact of the bill cannot be exactly determined. However, based on the estimates of state impact, the local impact would be between \$3 million and \$11 million.

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